Faster Payments Bridge Financial Inclusion

March 2023

According to The Committee on Payments and Market Infrastructures of the Bank of International Settlements (BIS), fast payments are defined as "payments in which the transmission of the payment message and the availability of final funds to the payee occur in real-time or near-real time, and on as near to a 24-hour and 7-day basis as possible."[1]

ESG stands for environmental, social, and governance (ESG). It describes a framework utilized by investors to capture the impacts of an organization's actions on its stakeholders. For example, ESG-motivated firms may adopt practices that benefit local communities, employees, or the environment.[2] According to the Securities and Exchange Commission (SEC), "ESG investing is a way of investing in companies based on their commitment to one or more ESG factors."[3]

We believe investors evaluating ESG factors in their investment strategies and decisions should consider investing in companies empowering financial inclusion. Faster payments advance the social goals of ESG principles, particularly when they are designed to facilitate financial inclusion.

Since 2006, when the Federal Deposit Insurance Corporation (FDIC) initiated its financial inclusion program,[4] many financial institutions have searched for the "killer app" that would bring unbanked households into the banking and payments system.

More than a decade later, there are many views on why millions of households prefer alternative financial services. Some contend that fears of paying overdraft fees have dissuaded low-wealth households from getting or keeping an account. Others contend that the unbanked will remain outside the banking system until banks can earn their trust. Another view holds that the unbanked will stay away until banks can match the price transparency and immediate funds availability offered by storefront check cashing centers.

In a 2018 speech, Federal Reserve Governor Lael Brainard said, "For these households, the difference between waiting for a payment to clear and receiving a payment in real time is not merely an inconvenience; it could tip the balance toward overdraft fees, bounced checks, or collections fees. To be clear, faster payments would not address the root causes of these households' financial fragility. Even so, faster payments could help reduce the strain on some."[5]

Ample evidence supports the view that payment delays create actual economic harm. IBISWorld reports that industry-wide revenues of check cashers and payday lenders exceeded $17.5 billion in 2022.[6] That year was not an aberration. In fact, from 2014-2022, industry-wide revenues of check cashers and payday lenders ranged between $15.7 billion and $17.8 billion.[7] Millions of Americans have sought alternatives outside banks in part because our payments system is too slow.

Enter faster payments. The Clearing House introduced its Real-Time Payments (RTP) platform in 2017,[8] and numerous other solution providers offer a faster payment service, one of which reported that account holders made 5 billion payments with a total value of almost $1.5 trillion in the first five years.[9] Several person-to-person (P2P) payment apps offer immediate payment services. With the expected introduction of FedNow in July 2023, more banks will add a faster payment option to their checking accounts. Inevitably, innovators will develop products to solve for the needs of the growing set of consumers and small businesses using faster payments. Currently scalable consumer-facing services exist, but typically only for those with a bank account. The increasing ubiquity of faster payment services for the banked raises an important question: how can faster payments reach the unbanked?

Outside the United States, numerous fast-growing digital wallets, such as Tigo Money, Oxxo® Pay, and TrueMoney, allow users to transact using only cash. These types of solutions allow unbanked consumers to transact digitally in-store and online. In fact, PIX, the faster payment system in Brazil, boasts over 100 million users and has been one of the primary P2P payment systems since its launch in 2020.[10] These wallets are poised to bridge the gap between the unbanked, banked, and faster payments.

An important additional consideration for unbanked U.S. consumers is whether a digital wallet is set up to provide deposit insurance to the consumer on the funds it holds.

P2P presents only one use case. In the future, many companies will build new solutions. It has been reported that over 50% of U.S. and U.K. retailers either accept or plan to integrate faster payments into their checkout.[11] In addition, Brazilian solution PIX has already surpassed bank card spending in the e-commerce environment and is expected to continue to grow in-store spending. No one can say how the U.S. market will evolve, but it's a certainty that the payment rails could be used to support sustainable and inclusive innovation. Overlay services built on top of payments infrastructure can support additional use cases and may present opportunities for profitable ESG investments.

One way companies can achieve their social goals is by fostering financial inclusion. A well-designed financial inclusion program can help people avoid an adverse financial cascade sparked by payment delays during a financial emergency, improve the social and economic fabric of communities, and serve as a catalyst to create more innovative and inclusive products and services that enhance financial well-being.

Other means for achieving the social goals include creating awareness, advocating for policy agendas, investing in community-based programs, and adopting direct and indirect investing and funding initiatives and innovations that leverage faster payments to drive more financial inclusion both by offering access and by including product design features that address the needs and concerns of those not yet financially included, such as concerns about account opening, transparency, fees, and prevention and remedies for mistake and fraud.

In recognition of these opportunities, the U.S. Faster Payments Council issued a report in July 2022[12] that discussed the needs for financial inclusion and identified steps that providers across the payment system can take to expand financial inclusion. The paper discusses how faster payments can address concerns, such as account opening requirements, overdraft risk and funds availability, that can keep consumers out of the banking system. Funds can only be sent if they are present in the account. Unlike with an ACH or a paper check, consumers have access to their funds immediately under system rules. The liquidity-constrained worker who pays to have their paycheck cashed to get cash right away to pay bills and avoid a late payment fee has no such obstacle if they can be paid with a safe, secure, optional faster payment. Moreover, current faster payment solutions in the market are either free to the consumer or come with lower costs than what they pay for in a check cashing store.

The paper emphasized the need for faster payment solutions in the U.S. that could match the best parts of cash, including its transparency and liquidity, with the flexibility and protections associated with electronic payments. It highlighted that the best services would inspire trust and be designed for the financial life of the underserved consumer. The paper also addressed areas of concern such as cost, mistakes and fraud, offering actions that private sector payments entities can take to alleviate these concerns.

Many existing and emerging frameworks help companies establish and measure their ESG goals. The Global Reporting Initiative Sustainability Reporting Standards (GRI)[13], the Sustainability Accounting Standards Board (SASB)[14], the United Nations Principles for Responsible Investment (PRI)[15], the United Nations Sustainable Development Goals (SDG)[16], and the World Economic Forum's International Business Council (WEF IBC)[17] all help to establish and provide guidance and measurement for ESG opportunities and risks.

The aggregated tenets of the groups mentioned above can guide how companies can support financial inclusion by incorporating an agenda for inclusive faster payments into a company's strategic planning and investment process to bolster their ESG goals, planned actions, outcomes, and measurements.

Some of the biggest burdens faced by underserved consumers include overdraft fees, short-term liquidity problems, and the high cost of alternative credit services to cover immediate needs. Faster payments can solve these hurdles directly, promoting inclusive and socially-minded growth. In addition, faster payment infrastructures create the foundation for innovators to develop inclusive solutions to allow the unbanked to engage, particularly if consumer trust and safety concerns are effectively addressed.

We encourage ESG professionals to read the U.S. Faster Payments Council white paper "Faster Payments and Financial Inclusion"[18] to learn more. For additional information about the U.S. Faster Payments Council visit https://fasterpaymentscouncil.org/ or email info@fasterpaymentscouncil.org.

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